

## Message Text

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ACTION ARA-20

INFO OCT-01 ISO-00 EB-11 SP-03 AID-20 NSC-07 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 CIAE-00

COME-00 FRB-02 INR-10 NSAE-00 XMB-07 OPIC-12 LAB-06

SIL-01 DODE-00 PA-04 USIA-15 PRS-01 L-03 DRC-01 /158 W

----- 004856

R 132030Z MAY 74

FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC 3282

INFO AMCONSUL RIO DE JANEIRO

AMCONSUL SAO PAULO

LIMITED OFFICIAL USE BRASILIA 3419

E. O. 11652: N/A

TAGS: EFIN, BR

SUBJ: CENTRAL BANK RAISES INTEREST RATES AND ADOPTS MEASURE

DESIGNED TO DIRECT FLOW OF FUNDS TOWARD INVESTMENT  
FINANCING

1. THE CENTRAL BANK OF BRAZIL HAS ANNOUNCED EFFECTIVE  
MAY 3 INCREASES ON INTEREST RATES ON TIME DEPOSITS,  
CERTIFICATES OF DEPOSIT AND BILLS OF ACCEPTANCE,

BRINGING THEM UP TO 24-26 PERCENT RANGE FROM THE  
21-23 PERCENT RANGE. IN ADDITION, THE MONETARY  
CORRECTION IS TO BE DETERMINED IN ADVANCE, I.E.,  
ACTUAL INTEREST RATE PAID TO BE KNOWN IN ADVANCE,  
ON DEPOSITS, CERTIFICATES OF DEPOSITS AND BILLS OF  
ACCEPTANCE WITH MATURITY OF UP TO 24 MONTHS. FOR  
INSTRUMENTS WITH MATURITY OF OVER 24 MONTHS, THE  
MONETARY CORRECTION IS TO BE DETERMINED AT TIME OF  
MATURITY (AND TO BE THE SAME AS THAT APPLIED ON  
TREASURY BONDS) I.E., ACTUAL INTEREST RATE PAID ON  
THESE INVESTMENTS WOULD NOT RPT NOT BE KNOWN IN  
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ADVANCE FOR PERIOD BEYOND TWO YEARS. THE BASIC

INTEREST RATE APPLICABLE AFTER THE 24 MONTHS  
(TO WHICH THE MONETARY CORRECTION IS TO BE ADDED)  
IS TO BE DETERMINED BY MARKET FORCES. CENTRAL  
BANK ALSO DECREED THAT THE SPREAD BETWEEN DEPOSIT  
RATES AND LOAN RATES FOR INVESTMENT BANKS CANNOT  
EXCEED SEVEN PERCENT, I.E., MAXIMUM INTEREST RATE  
ON LOANS MADE BY THESE BANKS CAN BE AS HIGH AS  
32 PERCENT. FOR THE FIRST TIME, THE CENTRAL BANK  
ALSO AUTHORIZED COMMERCIAL BANKS TO ACQUIRE FROM  
INVESTMENT BANKS, PARTICIPATING IN SAME CONGLOMERATE  
GROUP, CERTIFICATES OF DEPOSIT OR BILLS OF ACCEPTANCE,  
EITHER IN FORM OF NEW ISSUES OR AS CO-OBLIGATION,  
WITHIN CERTAIN NORMS SET BY THE CENTRAL BANK.

2. COMMENT: THE OBJECTIVES OF THESE MEASURES CAN  
BE SUMMARIZED AS FOLLOWS: (A) BY RAISING INTEREST  
RATES AND BRINGING THEM UP TO REALISTIC LEVELS, THE  
CENTRAL BANK HOPES TO ELIMINATE THE PRACTICE WHICH  
HAD APPARENTLY BECOME QUITE COMMON FOR FINANCIAL  
INSTITUTIONS TO PAY RATES ABOVE THOSE PREVIOUSLY  
PERMITTED BY THE MONETARY AUTHORITIES; (B) BY  
LIMITING PRE-FIXED MONETARY CORRECTION ON INSTRUMENTS  
WITH MATURITY UP TO 24 MONTHS, THE CENTRAL BANK  
WANTED TO PROVIDE A DISINCENTIVE FOR THE USE OF BILLS  
OF ACCEPTANCE OF LONGER MATURITY; THE CENTRAL  
BANK BELIEVES THAT FINANCIAL INSTITUTIONS WOULD  
BE HESITANT TO COMMIT FUNDS FOR PERIOD OVER TWO  
YEARS WHEN INTEREST RATE BEYOND TWO-YEAR PERIOD  
IS UNCERTAIN; SINCE THESE BILLS OF ACCEPTANCE  
ARE TIED TO CONSUMER CREDIT, CENTRAL BANK EXPECTS  
THIS MEASURE TO SLOW DOWN GROWTH OF CONSUMER CREDIT;  
(C) BY PERMITTING COMMERCIAL BANKS TO ACQUIRE  
CERTIFICATES OF DEPOSIT AND BILLS OF ACCEPTANCE  
FROM AFFILIATED INVESTMENT BANKS, CENTRAL BANK IS  
TRYING TO IMPROVE THE LIQUIDITY POSITION OF THESE  
LATTER INSTITUTIONS; THE CENTRAL BANK HAD HALLES  
GROUP EXPERIENCE IN MIND IN INTRODUCING THIS CHANGE;  
APPARENTLY THE LIQUIDITY CRISIS OF THAT GROUP  
EMANATED FROM ITS INVESTMENT BANK AND ALTHOUGH THE  
COMMERCIAL BANK WAS IN A POSITION TO HELP, IT WAS  
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FORBIDDEN TO DO SO UNDER THE THEN EXISTING REGULATIONS  
AND (D) BY DECREASING THE SPREAD FOR INVESTMENT  
BANKS FROM 8 TO 7 PERCENT, THE CENTRAL BANK HOPES  
TO STIMULATE EFFICIENCY.

3. THE CENTRAL BANK MAY BE TOO OPTIMISTIC IN ITS  
EXPECTATION WITH RESPECT TO ITS ABILITY TO CURB CONSUMER  
CREDIT THROUGH THE MECHANISM OF LIMITING THE PRE-FIXED

MONETARY CORRECTION ON BILLS OF ACCEPTANCE TO 24 MONTHS.  
THIS FOR TWO REASONS: (A) THE BRAZILIAN CONSUMER  
HAS BECOME ACCUSTOMED TO EASY CREDIT AVAILABILITY  
AND WILL ATTEMPT TO BORROW AS MUCH AS HE CAN ON  
TERMS OF 24 MONTHS, AND (B) THE PREVIOUS AVERAGE  
MATURITY OF BILLS OF ACCEPTANCE WAS REPORTED TO  
BE 18 MONTHS SO THAT ONLY SOME PORTION OF THE CREDIT  
WILL BE AFFECTED. IN ADDITION, THE CENTRAL BANK  
MAY HAVE INCREASED THE POSSIBILITIES FOR MONEY  
SUPPLY EXPANSION BY GIVING INVESTMENT BANKS ACCESS  
TO COMMERCIAL BANK LIQUIDITY. WHILE IN  
PRINCIPLE THIS LAST IDEA IS A GOOD ONE SINCE ITS  
OBJECTIVE IS TO INCREASE THE FLOW OF FUNDS INTO  
INVESTMENT BANKS, IT MAY MAKE IT MORE DIFFICULT  
FOR GOB TO KEEP MONEY SUPPLY EXPANSION AT THE PROJECTED  
35 PERCENT LEVEL IN 1974.  
CRIMMINS

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## Message Attributes

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